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Secretariat, Quality of Advice Review
Financial System Division
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Quality of Advice Review - Issues Paper

The Australian Financial Markets Association (AFMA) welcomes the opportunity to make comment on the Quality of Advice Review – Issues Paper (the Review).

We commend the Government for undertaking this review and for the important steps it has already taken towards making the accreditation and education requirements for financial advisors more flexible, efficient and better aligned with the needs of industry, investors and advisors.

For the advice problem to be addressed firms need to have ready clear mechanisms to allow them to provide general advice and non-comprehensive limited advice with being drawn inadvertently into the excessive demands of the current advice framework which treats all advice as if it were financial planning.

The Government must accept at this point with advice unaffordable for the many and thousands of advisors having left the system that it is not simply a lack of understanding on the part of thousands of businesses in regard to what is actually, in the view of the regulator alone, a workable system. The system is not workable. Substantial change is required.

To achieve the necessary improvements in advice availability and cost we support the following:

- **A comprehensive rebuild of the regulatory structures.**
- **A framework for scaled advice (if done correctly this could render advice categories unnecessary).**
- **A framework for digital advice.**

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- **A clear demarcation of general advice from personal advice, optimally a simple opt in or out for investors**.
- **Clear limits on the scope of the information the advice giver needs to consider when an investor limits advice to general advice or to only getting limited information, as opposed to personal advice. For common limited-scope scenarios such as SME FX, and stockbroking these requirements should be clearly defined**.

As we will discuss below, locating space for specialist advice providers such as stockbrokers, automated advice, scaled advice and SME FX providers offers ways of reducing costs and increasing options for retail investors.

Major change is required

A key risk for the review is taking a view that where the regulatory framework is currently at is a good starting point. It is not.

AFMA is concerned that the framing of some of the questions the Review is considering retains much of the financial planning focus of the current system and may not take a sufficiently clean sheet approach to be open to the range of potential outcomes that would be optimal, or even those that exist already.

While typically AFMA supports incremental change, the poor performance of the current arrangements suggests that major overhaul is required. Looking at other jurisdictions where advice is more accessible, and the range of risk cost options is broader is appropriate. Tweaking or piecemeal development of the current arrangements is unlikely to create the amount of change needed to deliver the outcomes sought by the Government and the Review. Our advice is: do not start from here.

We note the example of New Zealand which followed Australia's lead in introducing what its Parliament has referred to as "heavy regulation"[1] with similar distinctions to general and personal advice called "class advice" and "personalised advice". The results were the same: "Perhaps the most pressing issue, actually, at the moment in New Zealand is the sheer number of New Zealanders who simply don't receive any good advice at all."[2] Following an extensive review process that started in 2015 with an MBIE Options Paper, and legislation in 2019, in 2021 New Zealand replaced its regime moving to a lighter more flexible principles-based regime that is also designed to support robo-advice.

We do not suggest that the New Zealand outcomes are necessarily optimal for Australia, but the time committed, the process and commitment to comprehensive ground up rebuild when faced with similar issues is worthy of adoption in the Australian context.

Australia should look to learn from foreign schemes such as New Zealand and the US as they are likely to make better starting points for reform than the current Australian

[1] https://www.parliament.nz/en/pb/hansard-debates/rhr/combined/HansDeb_20180912_20180912_20

[2] *Ibid.* Michael Wood MP.

system. In relation to the US system, its separate treatment for brokers of financial products could well be worth local consideration.

Cost of Advice

As the review recognises, financial advice has been subjected to a large increase in regulation over many years. These regulations were well-intentioned and had the commendable aim to protect investors and lower their risk of receiving poor advice. While there is no doubt that change was required to improve practices in some parts of the industry, the build-up of reforms that resulted has loaded advice with duplicative, unworkable, and costly regulations.

This creates high costs for providers (and therefore investors), high risks for providers, higher barriers to entry, and services have been priced out of reach of most ordinary Australians.

The services that *are* delivered have multiple checks and balances to ensure they are not conflicted and are balanced and appropriate. For the great many Australians that would have benefited from prior arrangements but that are no longer in a position to receive financial advice, these improvements are of no benefit. Thus, a key failing of the system is therefore in the unmet demand for advice.

Many of these Australians still invest but are now more likely to do so on a self-directed basis. These investors are at risk of lesser investment outcomes impacting long term financial well-being and thereby placing a higher burden on the public purse unless action is taking to overhaul the regulatory framework to reflect the change to the retail market investor profile.

Firms no longer feel confident they are at all safe even simply providing accurate factual information about investments options and their risks. The high provider risk framework of the regulations combined with unhelpful court rulings mean that when somewhere in a distant unrelated department or business of a large firm some information is known about the investor then merely stating facts can lead to a presumption of personal advice, and failure to provide the full, costly, financial planning style assessment can leave the firm significantly exposed. This is an unmanageable set of affairs.

To ensure it meets its aims AFMA suggests that for any proposals its makes, that the Review models the likely impacts to financial advice costs and any expected decrease in the unmet demand for financial advice.

Recognising the breadth of services provided

As mentioned, **a key failing of the current scheme is that it has ignored the breadth of financial advice services provided by the industry and attempted to shoehorn all advice service provision into a financial planning model.** This was an ill-advised strategy and has resulted in significant disruption for the industry to the detriment of investors.

As we discuss in answer to the questions, comprehensive financial planning advice is demonstrably better than limited scope advice in the same way that a comprehensive

medical assessment is better in every way than a simple trip to the GP for a particular ailment. Except that requiring every trip to the doctor/financial advice provider to be a comprehensive medical/financial planning type advice creates an inefficient system that does not meet the needs of most people, makes risk reduction expensive and out of reach of many, and gives poorer systemic outcomes when considered across the whole population.

We are concerned that the Review should not head down a similar path. For example, when considering the question of accessible advice, the study by ASIC that is quoted is centred around experiences of, and decisions in relation to, the current financial planning focussed financial advice regime. This does not take into account non-financial planning advice, for example the foreign exchange advice provided to small and medium enterprises (SMEs) by specialised desks. Nor does it take into account types of advice that are now typically only provided in context of a broader relationship in this jurisdiction, such as ad hoc market advice.

A key example of the incongruity of this strategy was its application to SME FX advisors within the banks. These desks provide a vital economic service to the economy in the provision of FX services for small and medium businesses, typically for import and export purposes. These services allow firms to lock in profits on low margins without the risk of FX fluctuations making their transactions unprofitable. This increases their ability to compete internationally, and to provide cost effective goods locally.

Treating these advisors like financial planners has resulted in desks requiring advisors to train on superannuation, estate planning and insurance matters that are of no relevance to their clients or their business.

It has also pressured firms to hire from the financial planning graduate cohort as these graduates have the shortest path to productive work despite not having studied the most relevant subjects for the roles. We are very supportive of Treasury's ongoing work to create more flexible and appropriate pathways for these advisors.

We note that similar issues arise in relation to stockbrokers, who should be able to readily provide market commentary and trading investment ideas without considering the investor's superannuation needs.

Advice Efficiency

We see the way forward for the Government's policy on financial advice is to look at the subjective 'quality advice' from the more objective concept of 'advice efficiency'.

Advice efficiency is the degree to which advice-related risk is reduced per unit cost to the investor.

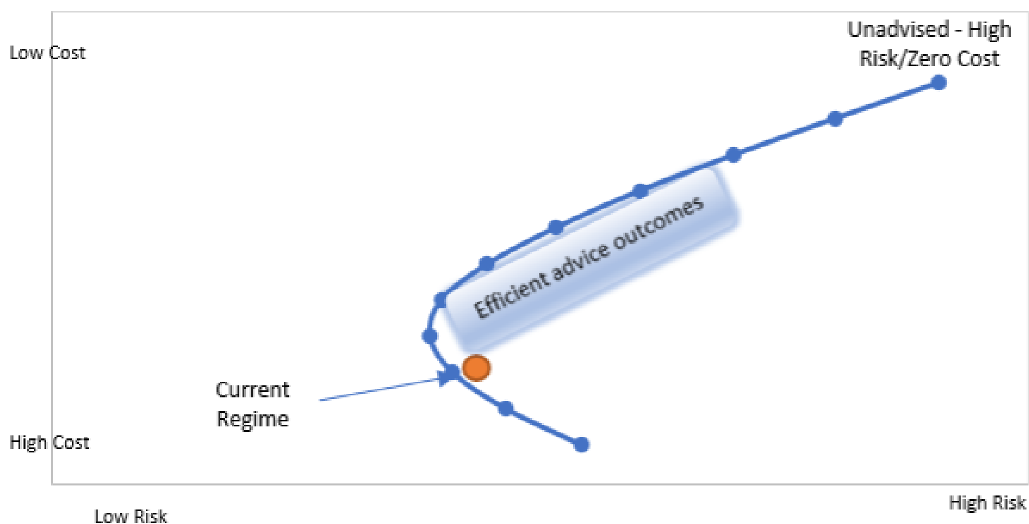
Investment advice aims to help investors achieve a desired exposure profile typically on or near the efficient investment frontier and thereby helps achieve their financial goals.

It is important to note that there is never any guarantee that the financial goals will be achieved, the 'outcome of the advice'/'return on their investments' in the Consultation Paper, as these are subject to risks that cannot be controlled by the advisor. For example, a conservative investment in a government bond still carries sovereign risk even for low risk governments. An advisor that placed a client into such a bond when the client requested a low risk investment would still have provided appropriate advice even if the government fell and the bond became worthless.

Advice may relate to a particular part of the investor's interest or to the investors overall financial planning. **Advice-related risk** is the risk that the advice, or lack of advice, within the scope of advice, fails to contribute appropriately to these goals.

When we consider advice-related risk vs regulatory-driven costs, there is often an efficient frontier where the 'returns' – in this case a lower incidence of advice-related risks - can be considered against what regulatory driven costs are created for investors and their portfolio returns. An efficient regulatory regime is one that gives investors many options close to this efficient frontier. There are a range of points along and near this advice-related risk vs cost curve that should all be considered efficient outcomes from a regulatory perspective.

We provide an indicative concept chart for the consideration of the Review. Note that at the upper end as costs increase (towards zero on the Y axis), advice costs can impact returns and thereby increase the risks to portfolio returns.



The Review states:

> More effective regulation may reduce the costs of compliance without prejudicing outcomes for consumers and, where there might be trade-offs between quality,

> accessibility and affordability, the Review will seek to determine whether the framework is achieving an *appropriate balance* between these elements.[3] [Emphasis added]

In our view the framework should allow a *range of efficient balances* between these elements to be achieved, rather than endeavour to select a *specific 'appropriate' balance* point.

Everyone is entitled in a free society to make investments without any advice and thereby without any protection, or with only the protection investors can provide for themselves. This means that the area to the very top right on the Concept Chart – that of one of the highest advice-related risks (no advice) and lowest cost (zero) will always remain an option.

There is certainly an argument that once investors do seek advice they should be able to expect they will not pay high costs for advice that does little to reduce (or even increase) advice-related risks. But this is not to say that their only option should be high-cost advice that provides low advice-related risk outcomes. **A range of cost outcomes should be available as long as these provide (reasonably) efficient advice-related risk reduction for the costs incurred.**

An analogy of the current arrangements might be that everyone is entitled to drive on the financial roads in a car they have built in their backyard no safety measures, but if investors do want to improve their safety the current regulations insist that only a high-end marque with the most advanced safety features will do, even though few can afford the upgrade, and most would prefer a middle ground option. The entirely predictable outcome is that many remain without any risk reduction.

Rather than merely trying to move the current regime upwards vertically to lower its costs and provide similar risk protections, there should be a broad range of efficient options provided in the blue zone highlighted in the concept chart.

Firms should be freed to compete to develop models that deliver efficient outcomes along, or near-enough to, the efficient frontier. It is important to be clear that this will mean expressly aiming for improved but not perfect outcomes. As long as the reduction in advice-related risk, be it large or more modest, is efficient per unit cost there is no reduction in the value offered to the investor.

To allow reductions in costs to be achieved may involve performing more limited analysis of an individual's circumstances – including limiting advice to an area of interest (e.g. which shares are performing well today), or considering a more limited range of investments, or perhaps suppliers of those investments.

[3] Quality of Advice Review, Page 4.

We note that while scaled advice is theoretically possible at present it is not practicable. It is currently too high risk for advisors to easily provide, as the regulatory requirements are vague and can be formed in hindsight. The regulations cannot be relied upon to protect advisors that do not undertake a full financial planning assessment of an investor, even when the investor may only want advice on a particular matter.

Conclusion

AFMA is concerned that the Review has not yet engaged with some of the well-known key issues relating to financial advice that require urgent action, including the need to recognise the diversity of types of financial advice providers and break from the current system's shoehorning of all advisers into a financial planning mould. We are also concerned that the Review is proposing yet more conflict avoidance requirements that could be damaging to capital formation in the economy and will not be in the interests of retail investors. **AFMA strongly cautions against impacting these capital raising activities.**

Finally, given that New Zealand faced similar issues and spent many years undertaking a comprehensive and cohesive rebuild of their financial advice laws we are concerned that **unless the Review recommends a more substantive process as a key outcome it may be difficult to complete a suitably comprehensive process that addresses our similar challenges by the December 2022 reporting date**. A process that rebuilds the framework from first principles drawing on the best practice internationally with local adaptations is advised.

We have provided responses to some of the consultation questions below. We thank you for considering our submission and would be pleased to assist with further information or clarification if required.

Yours sincerely

Damian Jeffree
Senior Director of Policy

Answers to consultation questions

Please find our answers to the consultation questions below. Some answers respond to question groups rather than individual questions.

Quality of Advice

1. What are the characteristics of quality advice for providers of advice?

Quality advice is advice that reduces advice-related risks on a cost-effective basis. See our letter above for further discussion.

As noted in our letter, return on investment is unsuitable as a measure of advice quality as it reflects the risk profile preferred by the investor and the outcomes of those risks.

Advice-related risks are numerous including knowledge and application of knowledge about relevant investment matters but are heavily dependent on the scope of the advice sought. For example, a small business looking to lock in FX for a future dated payment will have very specific advice-related risks. They could include knowledge of the trend and volatility of the FX pair in question, whether derivatives might provide an efficient solution and what a suitable rate is for the size needed. The quality will not depend on knowledge of estate laws, superannuation, insurance, etc.

For those seeking to invest small amounts say $5,000 into shares, quality advice would not include a comprehensive financial planning type assessment that costs $4,000. These costs might never be made back. Quality advice, for such a scenario, might include automated advice that can increase the knowledge and understanding of the investor and provide guidance on the types of investments that might be suitable given their risk appetite.

2. What are the characteristics of quality advice for consumers?

See our answer to question 1.

3. Have previous regulatory changes improved the quality of advice (for example the best interests duty and the safe harbour (see section 4.2))?

Please see the discussion in our letter above.

While the changes have increased the quality of advice that is still provided they have:

1) Cast all advice into a financial planning mould which does not suit many advice scenarios.
2) Created advice regulatory requirements that are not relevant for many advisors.
3) Created training requirements that are not relevant for many advisors.
4) Significantly increased the cost of advice which has made advice:
    a. inaccessible for many people; and
    b. unnecessarily costly for those that can afford it.

5) The requirements are inflexible and costly to implement and create unnecessary risks for firms.

4. What are the factors the Review should consider in deciding whether a measure has increased the quality of advice?

Stepping through individual measures and assessing them on one axis of impact is unlikely to lead to the balanced whole of system perspective that is required to reform the system in a way that delivers on the Review's mandate. An individual measure may well increase the quality of advice when considered in isolation but do so at a cumulatively unacceptable cost to the affordability or availability of advice.

The Review should look to understand how the requirements play out in a range of scenarios including in situations where more limited advice is sought or would be sought if it were available. In our view the current requirements place a substantial burden and risk onto firms wanting to provide anything less than a full financial planning assessment.

Missing from the assessment of quality is a system-wide assessment. i.e. What is the quality of advice across all those that potentially could seek advice and that currently do not seek advice – the unmet demand. Assessed on a system-wide basis the quality of advice of a regulatory system where large numbers do not receive any advice will be significantly lower than if the Review focusses on the quality of advice where it is delivered to those that can still afford it. Looking only at quality where advice is present may skew the analysis in line with the current system of requiring comprehensive advice with expensive safeguards.

Cost of Advice

5. What is the average cost of providing comprehensive advice to a new client?

6. What are the cost drivers of providing financial advice?

Costs drivers will vary depending on how the advice is provided, but will typically include staff, technology, compliance, back office, and management costs.

The scope of advice is also a determinant and the Review should consider how scope contributes to the cost of advice and can make advice more accessible.

7. How are these costs apportioned across meeting regulatory requirements, time spent with clients, staffing costs (including training), fixed costs (e.g. rent), professional indemnity insurance, software/technology?

8. How much is the cost of meeting the regulatory requirements a result of what the law requires and how much is a result of the processes and requirements of an AFS licensee, superannuation trustee, platform operator or ASIC?

9. Which elements of meeting the regulatory requirements contribute most to costs?

10. Have previous reforms by Government been implemented in a cost-effective way?

No. The current requirements are expensive to implement.

11. Could financial technology (fintech) reduce the cost of providing advice?

Yes.

With an appropriately accommodative regulatory framework financial technology could further reduce the costs of advice both where an advisor is involved and where the process is fully machine-based. General advice in particular can be provided much more efficiently through technology at scale.

12. Are there regulatory impediments to adopting technological solutions to assist in providing advice?

The current risks placed on firms by the advice regime are not conducive to optimising the amount of advice provided by technology. For example, where firms have data on an investor the provision of general advice that contains some knowledge (even isolated) might create a risk of the engagement being deemed personal advice.

Accessible advice

13. How should we measure demand for financial advice?

It is difficult to measure unmet latent demand, investor surveys might be one way forward.

14. In what circumstances do people need financial advice but might not be seeking it?

Investors may not be seeking advice because their investment amounts or budget do not warrant the costs associated with the current advice regime.

Investors may not be seeking financial advice because the type of scaled advice they would ideally like is not readily available.

Finally, investors may not recognise the potential benefit of financial advice and may gain an advantage from education about these benefits.

15. What are the barriers to people who need or want financial advice accessing it?

Customers often see financial advice as an involved process, more associated with personal financial planning, rather than business transactions or activities. A regulatory framework that is supportive of general and scaled advice would assist in making advice in more readily available, less expensive, smaller scale offerings. To enable firms to increase the availability of advice the risks for them would have to be lower.

Increasing the number of advisors will also help make advice more available. While out of scope for the Review we note that the current adviser accreditation pathways do not encourage individuals with subject matter expertise in financial markets to become an accredited adviser. Adviser education standards provide generalist education focused on financial planning. This is not a skill set sought out or valued by business owners seeking guidance on managing financial markets risk. Allowing sensible pathways for specialist advisors will assist increasing advisor numbers and the availability of advice.

16. How could advice be more accessible?

Regulations clearly defining and supporting the provision of scaled advice, digital advice, and general advice would allow advice to be more readily accessible. The provision of general advice could also be made more accessible by allowing targeted provision of information to customers. Increased utilisation of digital advice would also make advice more accessible.

17. Are there circumstances in which advice or certain types of advice could be provided other than by a financial adviser and, if so, what?

Yes, digital advice can provide effective solutions for a wide range of advice scenarios were there to be a sensible regulatory framework.

Minimum standards are important across the industry and AFMA supports the professionalisation of the industry.

While professional standards for financial advisers are out of scope, we note that there are some highly skilled individuals such as FX dealers industry accredited by AFMA that could readily provide financial advice in certain advice scenarios.

The nature of the FX transactions and products are relatively vanilla, and risk associated with the advice is confined to the transaction under consideration. This is very different to the nature of financial planning advice. For customers who are seeking advice on executing transactional FX (paying or receiving funds in a foreign currency for goods or services) or FX risk (the risk that exchange rates will move before a customer pays for their goods and change the outcome for a customer) industry accredited FX dealers would be well-placed to provide advice.

18. Could financial advisers and consumers benefit from advisers using fintech solutions to assist with compliance and the preparation of advice?

Fintech, while helpful, is unlikely to be a significant driver of improved affordability without a supportive regulatory framework.

19. What is preventing new entrants into the industry with innovative, digital-first business models?

Consistent with our comments above we note that it is hard to meet regulations for personal advice online and it is hard to be sure that the scope will be limited to delivering scaled advice or general advice. For digital advice to be compliant with the current requirements requires it to be too complicated and expensive for consumers to want to use.

Types of Advice

20. Is there a practical difference between financial advice and financial product advice and should they be treated in the same way by the regulatory framework?

There is currently effectively no practical difference between financial advice and financial product advice. The categorisation of a product as a financial product in the Corps Act drives the financial advice requirements.

We see value in separately treating financial planning type advice, and limited advice that relates to particular products – e.g. FX, shares and listed instruments.

These are very different functions that serve different purposes. Financial product advice is by nature limited advice with a specific scope and does not include matters like insurance, superannuation, and estate planning. We support the review looking at options to develop this approach drawing on international examples.

21. Are there any impediments to a financial adviser providing financial advice more broadly, e.g. about budgeting, home ownership or Centrelink pensions? If so, what?
22. What types of financial advice should be regulated and to what extent?

We are concerned that the proposal may be too incremental an approach retaining too much of the existing framework and retains a focus on the financial adviser type of financial advice rather than a broader recognition of the types of financial advice we have noted.

Moving where the line is drawn between personal advice and general advice while important is unlikely to be sufficient for a fully formed response to the issues of advice affordability.

There needs to be mechanisms for firms to be confident that they will not be inadvertently delivering personal advice. When providing advice under the current general advice model, a key risk is that the adviser when trying to assist the client, accidently provides personal advice by considering one of the client's objectives, financial situation or needs, for example, when discussing the expiry date of an FX Forward Contract and whether the customer need the ability to drawdown or extend. This type of assistance should not put the adviser at risk.

The regulations are targeted towards retail advice protections for individuals and are not a good fit for the very different needs and exposures of non-wholesale SME customers. For individuals seeking comprehensive financial advice, the nature of advice sought and required is generally more involved and complex as often they are discussing long term asset investments, that may impact their retirement or future financial plans. For businesses and corporates seeking FX advice the required advice is typically narrow in scope, as it is generally limited to cash flow, liability management and short-term funding requirements such as trade finance and foreign exchange contracts.

There needs to be options for investors to choose the right amount of advice-related risk reduction they wish to purchase.

23. Should there be different categories of financial advice and financial product advice and if so for what purpose?

Yes, AFMA very much welcomes consideration of the provision of other categories of financial advice to better reflect the reality of financial advice provision. Our focus in responding to this question below (adapted from a previous submission) is in relation to SME FX, but we also note the important role of stockbrokers in providing exchange market product-related advice.

Non-Speculative foreign exchange (FX) to retail corporate customer should be separated out from the Financial Advice Regulations, especially non-speculative or linear forwards with a short-term tenor (under 12 months).

1. Typical SME Client Example

The clients impacted by current rules are traditionally privately owned small to medium enterprise businesses. These businesses are captured by the "retail" definition under the Corporations Act.
As an example:

> A business imports light bulbs from China, which are then sold to a local Australian retailer.
> Each month the business negotiates a fixed USD price with their supplier and then pays 20% upfront and 80% in 90 days' time. To protect cashflow against FX market moves they work with their FX provider to lock in the USD purchase price in 90

days time. The business then settles this FX contract by sending a fixed USD amount to China to make the payment.

The current requirements are detrimentally impacting firms' abilities to provide these machine room SME transactions for the Australian economy. SME firms making these transactions require commercial understanding and broader preferably global business experience and no knowledge about superannuation, personal insurance and estate planning.

2. Issue

The fundamental flaw in the current approach was to try to shoehorn all retail financial market roles into a comprehensive financial planning model. This was never appropriate for many roles, notably FX forward providers to SMEs.

The industry is keen to work with the Government to find sensible ways forward that recognise that not all roles in finance fit into a 'planning' mould (and therefore require a knowledge of insurance and superannuation etc.).

We propose an approach below that will go some way to addressing the shortcomings in the areas of particular interest to AFMA members. We appreciate the complexity in managing the proposed changes and ask that they be considered in isolation of each other. If these require further refinement, we would be very open to working to that end.

3. Forward Exchange Contract Carve-out

Forward Exchange Contracts (FECs) are currently defined by the Corporations Act as a:

- "Derivative" under s761D(1) as read with regulation 7.1.04(1) of the Corporations Regulations 2001; and
- "Financial Product" under both s763A(b) as well as s764A(1)(c).

As a financial product, they are also captured as "relevant financial products" under s910A of the Corporations Act.

MiFID II: Financial instrument scope

In the European Union FECs are included as a MiFID financial instrument, but there are some important exemptions available specifically as it relates to FECs for the purposes of effecting payments.

Under MiFID II[4], any FX contracts that meet all of the criteria below are not considered financial instruments:

- It is a means of payment that:
  - Must be physically settled (other than by reason of default or other termination event).
  - At least one of the counterparties to the trade must be classified as a non-financial counterparty (NFC) as defined in EMIR[5];

[4] Commission Delegated Regulation (EU) 2017/565: Article 10(1)(b)
[5] Regulation (EU) No 648/2012

- The trade must be entered into to facilitate payment for identifiable goods, services or direct investment; and
- The trade is not executed on a trading venue.

The MiFID II recitals[6] provide further context:

> "Foreign exchange contracts may also be used for the purpose of effecting payment and those contracts should not be considered financial instruments provided they are not traded on a trading venue. Therefore, it is appropriate to consider as spot contracts those foreign exchange contracts that are used to effect payment for financial instruments where the settlement period for those contracts is more than 2 trading days and less than 5 trading days. It is also appropriate to consider as means of payments those foreign exchange contracts that are entered into for the purpose of achieving certainty about the level of payments for goods, services and real investment. **This will result in excluding from the definition of financial instruments foreign exchange contracts entered into by non-financial firms receiving payments in foreign currency for exports of identifiable goods and services and non-financial firms making payments in foreign currency to import specific goods and services.**"

As a result, if a non-financial firm enters into an FEC for purposes related to the payment of goods, services and investments, this would be excluded from the MiFiD II definition of a financial product.

We note that the UK FCA has also adopted a similar approach under its implementation of MiFID, providing further detailed guidance in its Perimeter Guidance Manual[7].

Proposed Approach

Similar to the MIFID II approach AFMA proposes that where physically settled FECs with a maturity of 12 months or under are used for payments purposes (and not for speculative purposes) they should be excluded from being financial products.

In the alternate it might be possible to create a carve out within section 7.6 definition of relevant adviser in the Corporations Act and allow industry accredited advisers.

Additional clarification

AFMA would also support greater clarity on when the financial product definition applies in relation to different settlement dates.

24. How should the different categories of advice be labelled?

There are a range of views on this topic.

25. Should advice provided to groups of consumers who share some common circumstances or characteristics of the cohort (such as targeted advertising) be regulated differently from advice provided only to an individual?

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[6] Commission Delegated Regulation (EU) 2017/565: Recital 10

[7] The Perimeter Guidance Manual (Chapter 13): Guidance on the scope of MiFID and CRD IV

Yes, targeted advertising to a group of relevant people is and should be permitted under other legislation (anti hawking). The nature of targeting advertising means a need or objective of that cohort of customers has been considered, however at present this potentially places the marketing in conflict with advice provisions as it may be captured as personal advice.

We believe that information presented to a group of customers should be regulated differently. Generally this would mean it should be made clear to each customer by the nature of the communication that they aren't the sole target or recipient of the communication/advice, and the intention would be to assist individuals make a decision themselves.

26. How should alternative advice providers, such as financial coaches or influencers, be regulated, if at all?

In general, consistent application of the rules across all advice providers is the best approach to avoid creating regulatory arbitrage opportunities, and given the same risks exist for conflicted or poor-quality advice from alternative advice providers, the same risk reduction framework should be applied.

While we agree that currently the restrictions on information and general advice are too restrictive for all providers including alternative advice providers, the solution is not to have carve out for different types of advisers or influencers as this will be confusing for investors, and unfair for providers.

27. How does applying and considering the distinction between general and personal advice add to the cost of providing advice?

At present providers will tend to err on the side of caution given the complexity of regulation and blurred line between general and personal advice – as we have noted this increases costs (and risks) to them and the investor. The current distinction cannot be readily relied upon from a risk perspective, pushing up the cost of all advice and discouraging the supply of general advice.

We also note that reduced user volume from the cost and complicated interfaces required from the unreliable distinction reduces the efficiencies of online advice. The risk of breaching regulations leads to onerous compliance requirements which also increase the cost of advice.

Intra-Fund Advice

28. Should the scope of intra-fund advice be expanded? If so, in what way?
29. Should superannuation trustees be encouraged or required to provide intra-fund advice to members?
30. Are any other changes to the regulatory framework necessary to assist superannuation trustees to provide intra-fund advice or to more actively engage with their members particularly in relation to retirement issues?

31. To what extent does the provision of intra-fund advice affect competition in the financial advice market?

Limited Scope Advice

32. Do you think that limited scope advice can be valuable for consumers?

Limited scope can be extremely valuable for investors.

The unworkable risks around limited scope advice are a key failing of the current regulatory arrangements and have led to significant dislocation in the industry.

Consistent with the ASIC research AFMA is of the view it is the vast majority of advice required and desired by investors. Very few want, need, or can afford comprehensive advice.

Limited scope advice can be of value where the nature of the advice required is limited to the type of activity the investor is interested in undertaking (for example, foreign exchange activities).

These activities are already confined by their nature to a narrower set of risks, outcomes and objectives for the customer. The advice in a particular area can be addressed in isolation of the broader circumstances of the retail investor.

Scaled advice is very different to the nature of comprehensive financial advice in the financial planning mould which may have focus on long-term outcomes and should have its own framework.

33. What legislative changes are necessary to facilitate the delivery of limited scope advice?

The analysis in the paper suggests that the current issue is "uncertainty within industry about how to provide such advice within the legislative framework". This is consistent with the ASIC view reported in the ASIC Affordable Advice Paper.

The industry is well-placed to judge the risks and soundness of the current allowances for scaled advice and despite economic incentives to make them work has been unable to do so.

This is not due to a lack of understanding on the part of the industry, which has a wide range of well-informed, highly experienced business people in its ranks. The industry view is firmly that the current arrangements are far from optimal in relation to scaled advice. At this point it is untenable for the regulator to claim that the framework for scalable advice is workable and the industry simply is not clear yet on how to work within it.

A framework is required in the Corporations Act specifically for scaled advice.

Major reform in the area of scalable advice is required. Scaled advice needs its own framework, and investors need to be able to limit the scope of advice and for there to be clear constrained limits on the scope of information (particularly for standard interactions such as FX and stockbroking) that the advice provider needs to consider.

At present when a small business approaches a bank for a forward dated FX contract an entirely unsuitable financial planning regulatory framework designed for individuals planning for retirement is applied in a cut-down form. The legal framework needs to recognise that firms and individuals should be able to approach FX providers and stockbrokers for domain specific advice.

We suggest that as there are some common scenarios that cover a large proportion of the non-financial planning space including FX and stockbroking that stating the requirements for these be clearly in the framework might be an efficient approach.

34. Other than uncertainty about legal obligations, are there other factors that might encourage financial advisers to provide comprehensive advice rather than limited scope advice?

There is a presumption in the question that comprehensive advice is preferable. This is not supported by the studies or the feedback from our members.

Comprehensive financial planning advice has a valuable role to play in long term financial health, but for most interactions more targeted work is appropriate.

There is an analogy to medical advice; a comprehensive health assessment is demonstrably better in every way than a single purpose trip to a General Practitioner. Yet having regular low-cost special purpose trips to the GP is likely more important to maintaining health than infrequent and expensive comprehensive assessments. At a population level supporting multiple special purpose trips is more efficient and keeps treatment accessible, and results in better population-wide outcomes.

An efficient system allows and supports both types of interactions and does not insist that only comprehensive financial planning is sufficient and acceptable.

Digital Advice

35. Do you agree that digital advice can make financial advice more accessible and affordable?

Yes. Digital advice has already made general advice (such as online broking) more widely accessible and affordable. Provision of digitally is also more economic for providers.

The revision of the regulatory framework to better integrate digital advice would assist in continuing this trend and would make digital advice more affordable and accessible to investors.

36. Are there any types of advice that might be better suited to digital advice than other types of advice, for example limited scope advice about specific topics?

Yes. Investment advice is well suited to digital being as it has a defined scoped and has a large component of generic information provision and education.

37. Are the risks for consumers different when they receive digital advice and when they receive it from a financial adviser?

The same risks largely apply to digital as to face to face advice. Digital advice has lower cost, but with current technology may not be as agile as in person advice in exploring investor needs. Acknowledgement of the limitations and benefits of the advice by the investor would seem a reasonable control.

38. Should different forms of advice be regulated differently, e.g. advice provided by a digital advice tool from advice provided by a financial adviser?

There are some differences in what is needed to manage the risks of digital advice provision (e.g. conflicts and best interest duties) but principles-based regulation that is appropriately accommodative should enable these differences to be managed by firms.

39. Are you concerned that the quality of advice might be compromised by digital advice?

No. Digital advice has an important role to play and properly utilised will not compromise the quality of advice. This is true for both individual application and when considering the system as a whole where it could significantly contribute to addressing unmet advice demand.

At present AFMA members are concerned that the majority of retail investors are either not getting advice, or enough advice; the wider provision of digital guidance and digital advice would be a significant improvement with minimal risk if properly managed.

While digital advice provision might in some circumstances not be as comprehensive as that provided by a comprehensive financial planning type assessment this does not detract from its efficiency in reducing advice-related risks, particularly when its lower cost and wider availability is considered. Both digital advice and financial adviser advice can help the investor to invest for the long term with a consistent asset allocation and disciplined approach.

40. Are any changes to the regulatory framework necessary to facilitate digital advice?

While the existing rules allow for digital general advice, they are not sufficiently clear around where the border is with personal advice.

We suggest a framework for scaled advice that clearly states that:

- Comprehensive advice and associated broad fact finding is not required for limited scope advice – clear simple scope should be sufficient for many transactions such as those in FX and stockbroking.
- The scope can be defined and limited by the investor, including to standard scope options such as FX and stockbroking.
- Existing information known need not be used if it is beyond the scope of the advice; and,
- General advice is suitable for limited scope personal advice.

41. If technology is part of the solution to making advice more accessible, who should be responsible for the advice provided (for example, an AFS licensee)?

An AFSL licensee.

42. In what ways can digital advice complement human-provided advice and when should it be a substitute?

Digital advice can complement human-provided advice by being a low-cost easily accessible delivery channel as part of a service where access to human advisers is available if required or on a limited basis. Such hybrid models – online and limited human advice - have been successful in the United States allowing the investor to ask more complicated questions of human advisers and gain the benefit of a personal connection.

Digital advice can also substitute human-provided advice by providing a low cost, easy, accessible option for those that choose it over face to face.

The choice should be investor driven and while there will be a cost difference, both human-provided and digital advice can be efficient ways of reducing advice-related risk.

Best Interests and Related Obligations

43. Do you consider that the statutory safe harbour for the best interests duty provides any benefit to consumers or advisers, and would there be any prejudice to either of them if it was removed?

Advisers have a vested interest in doing the right thing by clients and providing appropriate advice.

The ‘safe harbour steps’ are a way an adviser can demonstrate they have compiled with the best interests duty, but the current requirements may incentivise being able to evidence completion of the ‘safe harbour steps’ as opposed to focusing on the intent and

overall goal of the best interest duty. As referenced in the Review Paper, we believe the principles-based approach would be a better option especially when providing advice in relation to a client's foreign exchange needs.

Competent advisers will always consider the customer's best interests when providing personal advice and using a principles-based approach would allow firms to create a more efficient approach to providing personal financial advice. It should allow advisers to provide quality advice without focusing on being able to demonstrate that they have satisfied each step of statutory safe harbour steps, which can be time consuming and therefore expensive.

In the US, rather than using step-by-step safe harbour provisions the regulations require a principles-based approach with the broker following four specified obligations: the disclosure obligation, the care obligation, the conflict-of-interest obligation, and the compliance obligation.

Under this approach the adviser is driven to consider the overall provision of advice to make sure they are acting in the client best interest rather than a formulaic process.

44. If at all, how does complying with the safe harbour add to the cost of advice and to what extent?

In addition to the time spent by the adviser, there are also the resources used to monitored ensuring the advice meets the 'safe harbour steps'. The monitoring process will generally be structured on each of the safe harbour steps and ensuring the advice meets each of those requirements and also a consequence management framework that incorporates non-compliance with the 'safe harbour' requirements.

45. If the safe harbour was removed, what would change about how you would provide personal advice or how you would require your representatives to provide personal advice?

We believe that if the safe harbour steps were removed, the advice provided could still be appropriate and achieve the overall objective of meeting the client's best interests. The change would support a shift from meeting specified steps to considering principles and this would support delivering strong customer outcomes.

46. To what extent can the best interests obligations (including the best interests duty, appropriate advice obligation and the conflicts priority rule) be streamlined to remove duplication?

Further amendments are required on the 'Conflicts priority rule', when providing financial advice to retail clients. Conflicts are often unavoidable and sensible arrangements should allow them to be managed or disclosed.

47. Do you consider that financial advisers should be required to consider the target market determination for a financial product before providing personal advice about the product?

TMDs exist to ensure products are suitable for the target market they are intended to assist guide primary issuance.

We believe the best interests duty of financial advisers means that they should be free to recommend a product to a customer outside of the target market provided the product meets the customer's requirements and is in the customer's interest.

Conflicted Remuneration

48. To what extent has the ban on conflicted remuneration assisted in aligning adviser and consumer interests?

A comprehensive review of the interaction of the ban on stamping fees and its interaction is beyond the scope of this submission.

We note that AFMA opposed the removal of the ban on stamping fees in relation to Listed Investment Companies and Listed Infrastructure Trusts. The entities underlying LICs and LITs have played an important role in capital formation and investment in Australia for many decades. New entrants will face more difficulty raising capital now that stamping fees have been banned for these instruments.

We note that one of the concerns that drove the change to LICs and LITs was the underperformance of the sector. We noted "the ASIC analysis also gives emphasis to recent year performance. For long term investments this may not be an appropriate approach". Since that time with the changed market conditions the sector rallied over 30% in FY 2021. Trading levels relative to NTA also returned to more historical levels.

49. Has the ban contributed towards improving the quality of advice?

As we have noted changes in advice requirements over the last 20 years have resulted in an inefficient costly and inaccessible regime. While the regime, taken as a whole, has helped to ensure that for those that can afford the available advice it has lower advice risks, this should not be taken to mean that the requirements are an efficient or appropriate solution.

As per our concept chart investors should be able to access a wider range of advice-risk reduction opportunities outside the narrow comprehensive advice path that is available at present.

The Review is asking the wrong question. AFMA supports good conflicts management but has consistently opposed the ill-informed FASEA approach of an outright ban on acting where there are conflicts. Other jurisdictions, again notably New Zealand, have sensible

accommodations to the in many cases unavoidable conflicts that form part of service provision in a market economy.

FASEA sought to introduce an unsustainable distinction, not supported by any legal precedent and in our view clearly in error, that an 'actual conflict' exists only where a conflict inappropriately influences action. FASEA attempted this redefinition of the concept of conflict of interest as it recognised that there are unavoidable conflicts but also that the industry still needed to function.

Rather than look to extend the bans on conflicted remuneration which would appear to have contributed to the issues the Review has been tasked with solving, the Review should be asking whether the current management of conflicts contributes to an optimally balanced outcome. As we will discuss in response to Question 51 below the proposed extensions risks significant economic harm to the economy and further restrictions on the service provisions to retail clients. We suggest that the Review look to remodel the conflicts management regime based on the New Zealand approach.

50. Has the ban affected other outcomes in the financial advice industry, such as the profitability of advice firms, the structure of advice firms and the cost of providing advice?

The ban has led to substantial structural changes in the industry that have reduced the availability of advice, the range and affordability of services offer to retail investors.

51. What would be the implications for consumers if the exemptions from the ban on conflicted remuneration were removed, including on the quality of financial advice and the affordability and accessibility of advice? Please indicate which exemption you are referring to in providing your feedback.

Benefits of capital raising

Capital raising through the financial markets is a critical function in market-based economies and is of direct benefit to companies, investors, governments and the broader economy.

The contribution of retail investors to capital market raising overall is significant but will vary for different capital market products and the economic period and investor appetite in which the raising takes place.

The stamping fee exemption facilitates the wide distribution of capital raisings to retail investors. Capital raisings can be very work-intensive undertakings, particularly in the case of large placements and privatisations.

The considerable amount of work by firms involved benefits those seeking to raise the funds, the companies involved, the owners of the companies (including from time to time the Government through privatisations), and the retail investors who are able to gain exposure to a wider range of investment opportunities.

The products to which the remaining stamping fee exemption applies have continued to serve the economy well, providing ample capital to companies, to banks through hybrid issues, and to real estate managers through the Real Estate Investment Trust (REIT). They have also benefited infrastructure owners and projects with the provision of capital through infrastructure securities, and to governments through privatisations.

AFMA strongly cautions against impacting these capital raising activities.

While the loss of stamping fees for LICs and LITs is regrettable and creates inconsistencies, it was not expected to significantly harm the economy.

Removal of the stamping fee exemption for the other products we have listed, however, could risk far more significant economic harm. We caution against interfering with the ability of the private sector to raise capital through regulatory fixing of the price for these services at zero in a market-based economy

Removal of the exemptions to the ban on conflicted could be significantly damaging to the ability of firms to raise capital and thereby to the Australian economy.

While institutional capital dominates at the larger end of the market, for small stocks retail investors play a proportionately more significant role. Retail capital is often critical in assisting small companies get off the ground.

There is a substantial amount of work required for prolonged periods of time in the IPO distribution process and the removal of stamping fees would likely reduce the number of brokers distributing IPOs.

Brokers are commercial operations and should be able to profit in a market economy from undertaking economically productive work.

Retail clients would have less access to primary market capital raisings and would be increasingly confined to the secondary market. Investors buying on the secondary market would have to pay brokerage which is not the case on primary markets and would also miss gains in price made from the IPO price which are typically at a discount to subsequent trading.

As part of the listing admission criteria, a company requires a minimum of 300 non-affiliated investors which will be harder to achieve with less retail investors in primary markets. This could ultimately reduce the amount of companies that list and are available to investors on the secondary market.

52. Are there alternatives to removing the exemptions to adjust adviser incentives, reduce conflicts of interest and promote better consumer outcomes?

We do not believe the case has been made for further interventions in relation to adviser incentives and caution against damaging the capital raising abilities of the Australian market.

53. Has the capping of life insurance commissions led to a reduction in the level of insurance coverage or contributed to underinsurance? If so, please provide data to support this claim.
54. Is under insurance a present or emerging issue for any retail general insurance products? If so, please provide data to support this claim.
55. What other countervailing factors should the Review have regard to when deciding whether a particular exemption from the ban on conflicted remuneration should be retained?

The Review should have regard to the potential for significant impairment to the capital raising abilities of the financial markets and thereby the potential for economic impairment.

Charging Arrangements

56. Are consent requirements for charging non-ongoing fees to superannuation accounts working effectively? How could these requirements be streamlined or improved?
57. To what extent can the requirements around the ongoing fee arrangements be streamlined, simplified or made more principles-based to reduce compliance costs?
58. How could these documents be improved for consumers?
59. Are there other ways that could more effectively provide accountability and transparency around ongoing fee arrangements and protect consumers from being charged a fee for no service?
60. How much does meeting the ongoing fee arrangements, including the consent arrangements and FDS contribute to the cost of providing advice?
61. To what extent, if at all, do superannuation trustees (and other product issuers) impose obligations on advisers which are in addition to those imposed by the OFA and FDS requirements in the Corporations Act 2001?
62. How do the superannuation trustee covenants, particularly the obligation to act in the best financial interests of members, affect a trustee’s decision to deduct ongoing advice fees from a member’s account?

Disclosure Documents

63. How successful have SOAs been in addressing information asymmetry?

The SOAs have provided a high cost pathway to addressing information asymmetry for comprehensive advice. AFMA holds that this was being provided by most advisers in various methods prior to the regulations coming in a way that was lower cost, less formulaic, and more tailored to the client’s needs and understanding.

Due to the specific requirements on the adviser and licensee SOAs are too heavily burdened by various disclaimers blurring the more important, relevant information for the customers. For example, an SOA being provided to retirees could end up being more than 80 pages. If the FSG and Terms of Engagement (ToE) are robust, the SOA could be more succinct, relevant for purpose and better for the customer.

SOAs or their equivalents need to be taken into account when designing a scaled advice regime. Less onerous SOAs for scaled advice can create significant efficiencies.

Members also note the grey in the ROA vs SOA determination, similarly around amendments of SOA vs requiring a new SOA.

64. How much does the requirement to prepare a SOA contribute to the cost of advice?

Around 25 to 30% of the time required to complete a customer engagement is taken up with the preparation and presentation of the SOA.

Licensees have had to decide to increase the cost of advice to counter reduction in clients advised or to take on additional headcount leading to overall reductions in net profit.

65. To what extent can the content requirements for SOAs and ROAs be streamlined, simplified or made more principles-based to reduce compliance costs while still ensuring that consumers have the information they need to make an informed decision?

The issue is less about reducing costs (as many parts of the SOA are templated / locked content) but more about the accessibility, useability and understanding of the document for the client.

The SOA in its current format is a regulatory focussed tool rather than ensuring the customer's understanding.

The industry needs a singular, simple, document that serves the client. Providing description of needs, covering off fact find and presenting solutions and alternatives and detailing costs. The remaining required parts of the SOA should sit in either the FSG or ToE.

66. To what extent is the length of the disclosure documents driven by regulatory requirements or existing practices and attitudes towards risk and compliance adopted within industry?

The extent to which the above is documented is driven by the requirements of safe harbour. Advisers and licensees are required to create a document for regulatory

purposes rather than providing the best possible document for the client (which would be their preference).

67. How could the regulatory regime be amended to facilitate the delivery of disclosure documents that are more engaging for consumers?

By simplifying the advice document, enabling advisers to refer or link to all the additional standard disclosures.

Enabling the disclosure documents to be issued as web-based links would save the licensee both time and costs, especially when updating. There are issues that need to be addressed such as being able to record the version that the client saw when initiating any engagement and web-based solutions are not always the most appropriate for the most vulnerable, the elderly or those with limited capability.

68. Are there particular types of advice that are better suited to reduced disclosure documents? If so, why?

We propose that liability based, non-speculative, FX advice with tenor of less than 12 months should allow for reduced disclosure documentation.

Liability based advice in FX generally uses directly comparable products, consistent in both their terms, operating model, cost, and outcome. Average tenor is less than 6 months with a negligible proportion over 12 months. Cash flow-based risk management protecting the business as opposed to exposing them to increased risk.

We feel there is a need to redefine general advice and the products and services that are captured under the regulations.

69. Has recent guidance assisted advisers in understanding where they are able to use ROAs rather than SOAs, and has this led to a greater provision of this simpler form of disclosure?
70. Are there elements of the COVID-19 advice-related relief for disclosure obligations which should be permanently retained? If so, why?

Accountants Providing Financial Advice

71. Should accountants be able to provide financial advice on superannuation products outside of the existing AFSL regime and without needing to meet the education requirements imposed on other professionals wanting to provide financial advice? If so, why?
72. If an exemption was granted, what range of topics should accountants be able to provide advice on? How can consumers be protected?

73. What effect would allowing accountants to provide this advice have on the number of advisers in the market and the number of consumers receiving financial advice?
74. Is the limited AFS licence working as intended? What changes to the limited licence could be made to make it more accessible to accountants wanting to provide financial advice?
75. Are there other barriers to accountants providing financial advice about SMSFs, apart from the limited AFSL regime?

Consent Arrangements for Wholesale Client and Sophisticated Investor Classification

76. Should there be a requirement for a client to agree with the adviser in writing to being classified as a wholesale client?

There are a range of views on this question.

Members note the difficulties of clients moving in and out based on the number of employees test and other criteria. Point in time tests with the current arrangements have little to no enduring value. For firms with a large customer base this process can be unmanageable.

An improvement would include having a way of creating a more enduring period of classification certainty.

77. Are any changes necessary to the regulatory framework to ensure consumers understand the consequences of being a sophisticated investor or wholesale client?

A standard disclosure statement to provide the investor would be useful setting out the consequences for investors that providers can utilise.

The industry would support working with the government on standard wording to support advising customers of the protections they do not have access to as a wholesale customer to increase consistency.

78. Should there be a requirement for a client to be informed by the adviser if they are being classified as a wholesale client and be given an explanation that this means the protections for retail clients will not apply?

There are a range of views on this question.

Other measures to improve the quality, affordability and accessibility of advice

79. What steps have licensees taken to improve the quality, accessibility and affordability of advice? How have these steps affected the quality, accessibility and affordability of advice?

80. What steps have professional associations taken to improve the quality, accessibility and affordability of advice? How have these steps affected the quality, accessibility and affordability of advice?
81. Have ASIC's recent actions in response to consultation (CP 332), including the new financial advice hub webpage and example SOAs and ROAs, assisted licensees and advisers to provide good quality and affordable advice?
82. Has licensee supervision and monitoring of advisers improved since the Financial Services Royal Commission?
83. What further actions could ASIC, licensees or professional associations take to improve the quality, accessibility or affordability of financial advice?

While we acknowledge that advisor accreditation is out of scope for the Review we include these comments for context as advisor professionalism forms an important part of the solution to advice.

As noted in the Quality of Advice issues paper the top three areas investors want advice are investments (45%), retirement planning income (37%) and superannuation (31%).

It is unlikely that advice in relation to a client's foreign exchange needs falls into any of these categories as the majority of FX transaction executed are less than a year and the actual tenor is more likely to be three months and relate to hedging trade terms and not speculative trading.

Due to the very specific market that SME FX providers service there is a need for some further refinements to the education requirements for FX Market Specialists.

FX Markets Specialists largely hold 'relevant' degrees as defined by the FASEA legislation at an AQF7, 8 or 9 level across areas such as Business and Finance, but only a small minority will hold an 'approved' degree. The relevant degrees that these individuals hold is typically far more pertinent and helpful to their roles than the planning type degrees on the FASEA approved list.

The FASEA exam and approved degree framework is focussed on issues relevant to financial planning and does not cover matters relevant to those working in financial markets or looking to advice customers on financial markets specific products. This reduces accessibility of advice, as few accredited advisors have sufficient experience in financial markets to provide useful specialist advise to customers in matters such as foreign exchange risk.

We propose a new category of adviser - 'Market specialists' for foreign exchange - be created within the advice framework. This category should be limited to providing advice in relation to market products and activities, and should not cover insurance, superannuation, estate planning etc.

We propose that for this category of adviser the approved degree requirement could be met by a combination of an undergraduate degree or higher, plus the AQF 8 level courses required for AFMA Accreditation (currently available from Macquarie University but

potentially others) plus the FASEA Ethics course or equivalent (we note the AFMA course includes an integrated business ethics course).